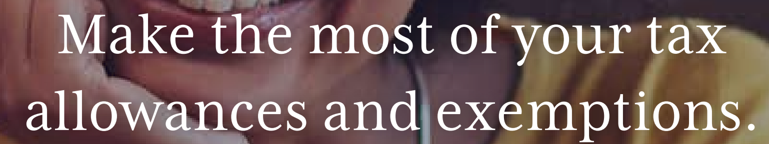
CHARLES STANLEY
*Wealth Managers*

*Focusing on you*

# 2020/21 Tax Year Guide



Make the most of your tax allowances and exemptions.

An introductory guide to the key allowances and limits for the 2020/21 tax year.

Please note this guide outlines many of the most important tax allowances and financial planning issues, but it is a short summary and not intended to cover all subjects. In addition, it does not take account of individual circumstances, which can vary a great deal. We strongly advise working with a financial planner who can make appropriate recommendations based upon your circumstances.

# About Charles Stanley

Charles Stanley is an award-winning Wealth Management firm. Since 1792, we've been helping our clients, including private individuals, families, charities and trustees, achieve their financial goals.

While others put their clients in categories, experience has taught us to take a personalised and holistic view. We explore every aspect of your financial world – ambitions, concerns, attitude to risk, and preferred way of working.

# **Personal Financial Planning:** Our speciality

We look objectively at your plans, applying a long-term view to provide a solution that works for you as priorities change over the years. We offer so much more than financial advice: we deliver tailored, joined-up and complete lifestyle planning. We aim to give you peace of mind – and a plan that you can look forward to.

This guide aims to give you a greater insight into the various ways to save tax. Tax efficiency is an important part of growing and preserving wealth and plays a vital role in creating a financial plan.

# ISA Allowance

If you are thinking about investing or considering a more tax efficient way to save money, Individual Savings Accounts (ISAs) are a great choice. They are flexible and free from Income and Capital Gains Tax (CGT).

There are several different types of ISA:

- Cash
- Stocks and Shares
- Lifetime
- Innovative Finance ISA
- Junior ISA

By using your annual ISA allowance, currently £20,000 for 2020/21, you can build up a significant pot of money free from Income and CGT.

Anyone who is UK resident can take out an ISA. If you are aged 16 and over, you can open a Cash ISA and from the age of 18 this can be a Stocks and Shares, Lifetime or Innovative ISA.

## Cash ISA

A Cash ISA is a savings account with interest payable which can be fixed or variable. A Cash ISA is a good way of building up an emergency fund as it is low risk. Interest rates are low, so this type of ISA will not provide a lot of growth compared to investments where your capital is at risk.

## Stocks and Shares ISA

You can invest in shares, funds, investment trusts or bonds within this type of ISA. This is a longer-term investment and your capital is at risk due to the underlying investments. This type of ISA has potential for long term growth.

## Lifetime ISA

This type of ISA helps you save for your first home (or retirement). If you are between the age of 18 and 39 you can contribute £4,000 per annum and the government will add a bonus of 25% (up to £1,000). There are strict rules around this type of ISA, so please speak to a financial adviser. The £4,000 investment forms part of your overall £20,000 ISA Allowance.

## Innovative Finance ISA

This is for peer to peer lending and investments. You use your ISA allowance to lend directly to others via the peer-to-peer lending market. The rates of interest can be generous, however your capital is at risk.

## Junior ISA (JISA)

If you are the parent or legal guardian of a child under 16 you can take out a Junior ISA for them, if they are 16 they can take it out themselves in addition to a Cash ISA (£20,000). The current allowance is £9,000. This is a great way of building up a lump sum for their future. A JISA can be a Cash ISA or a Stocks and Shares ISA. Anyone can add money such as a grandparent, however only the child can withdraw from the JISA from the age of 18 and at this age the JISA becomes an ISA.

Please speak to a financial planner who can provide advice on the most suitable ISA for your needs.

## Did you know?

Dividend allowance was cut from £5,000 to £2,000 in 2018.

# Inheritance Tax: Simple ways to reduce the size of your estate

Inheritance Tax (IHT) is a tax on an individual's estate on death, taxed at a rate of 40% on the excess over the Nil Rate Band (NRB) – currently £325,000. It is possible to transfer any unused NRB to a spouse/civil partner upon death – meaning there is no IHT due on the first £650,000 of assets.

A "Residence Nil Rate Band" (RNRB) of £175,000 per individual can also be claimed upon death, provided an individual's main residence passes to direct descendant(s). The RNRB is only available under certain circumstances but means that potentially an estate of up to £1 million can escape IHT.

There are several ways in which an IHT liability can be reduced during lifetime, including the gifting of assets (either directly or via a Trust). A few exemptions are also available, including gifting out of regular income and an annual £3,000 gifting allowance.

A simple way to reduce the size of your estate, and a potential IHT bill, is to gift money to others, perhaps children or grandchildren to help them out financially. Gifts exempt from IHT include an annual £3,000 lump sum, which can be given to one person or divided between a number of people, plus £250 a year to as many people as you like.

# Gifting larger sums

Any outright gifts to individuals or certain trusts have the potential to be exempt from IHT too. A 'Potentially Exempt Transfer' (PET) is a gift or transfer exempt from IHT where the individual survives for at least 7 years. If the individual dies within the period, it becomes a 'Chargeable Transfer' for IHT purposes and will be taken into account in the individual's IHT calculation on death. Any such gifts that add up to more than the nil-rate band of £325,000 are chargeable.

Through careful planning it is possible, to gift sums at an opportune time, or at various stages, to make use of the nil-rate band through an appropriate means, for instance using a discretionary trust to retain control over who benefits from the money and when. There are also other types of trusts that allow you to receive some income or capital. This is a complex area so please speak to a financial adviser.

# Capital Gains Tax Allowance

Capital Gains Tax (CGT) is a tax on the profit when you sell or dispose of an asset that's increased in value – unless it is in a tax efficient wrapper such as an ISA or pension.

You can pay CGT on profits from the sale of:

- Investments
- Shares
- Land
- Second property

You are exempt from CGT on things like

- Your main residence
- ISAS
- Pensions
- VCTs
- EIS Investments

Everyone has an annual CGT allowance, in 2020/21 the allowance for individuals is £12,300 and £6,150 for trusts

The rate of CGT chargeable is usually 10% for a basic rate taxpayer and 20% for a higher rate tax-payer however for Investment, buy to let or second properties the rates are 18% and 28%.

**How do I reduce my CGT bill?**

- Offset losses against profits
- Transfer to spouse
- Reduce taxable income

**When do you pay?**

You must declare any CGT liabilities on your Self-assessment for the same year and this must be settled no later than the 31st January in the following year. However, from April 2020 any liability relating to the sale of an investment property must be settled within 30 days of the date of sale.

It is not possible to carry the CGT allowance over to the next tax year. Therefore, if you are plan-ning to sell assets that have gone up in value more than your capital gains tax allowance, it may make sense to split this over more than one tax year.

CGT is a complicated tax and it is important to take advice on this subject.

# Bed & ISA and Bed & SIPP

One way to help use up your ISA allowance is using investments you own outside an ISA through a process known as a 'Bed & ISA'. This involves selling holdings and then buying them back simultaneously within the ISA wrapper. The sale crystallises any capital gain or loss made, so selling or partially selling an existing investment could help with tax planning by using some of your capital gains allowance, while keeping your holding.

You can make gains of up to £12,300 this 2020/21 tax year free of Capital Gains Tax (CGT), but should this allowance be exceeded CGT would become payable. If you generate a loss on a sale, and you declare this on your tax return, this could be carried forward to offset against capital gains in future years.

Once inside an ISA, though, any future gains on the investments are free from CGT and there is no further tax to pay on any income. As well as harvesting capital gains while maintaining existing investments, a Bed & ISA can be used to tidy up small or non-tax-efficient parts of your portfolio or make more of neglected holdings. It could also reduce the work required to complete your tax return.

A 'Bed & SIPP' offers a similar technique with using a pension. The added bonus is income tax relief (see the pension section) without investing any new money.

# Pension contributions

Almost everyone includes a comfortable retirement as one of their financial goals. Pensions are often a highly effective means of achieving this due to the tax relief available on payments into them.

Currently, anyone under 75 with relevant UK earnings can receive tax relief when they make a contribution within the annual allowance to a personal pension. 20% is added by HMRC and any further higher or additional rate income tax relief can be reclaimed – potentially a simple way of reducing your income tax bill for the year.

For example, an investor contributes £8,000 into their SIPP and £2,000 is claimed back from HMRC by the pension provider.  A higher rate tax payer could claim back up to a further 20% via their tax return, reducing the overall cost of the contribution to as little as £6,000. In the same instance, additional rate tax payers could claim back up to a further 25% making the cost just £5,500 for a £10,000 contribution. Please note that rates of income tax and relief differ in Scotland.

Tax relief on your personal contributions is limited to 100% of your relevant UK earnings. Contributions, including those paid by your employer, are also subject to the annual allowance, which for the 2020/21 tax year is usually £40,000. However, those with 'adjusted' income (broadly speaking income plus pension contributions from employers) over £240,000 for this tax year can have a reduced annual pension allowance, the minimum being £4,000.

# Pension contributions continued

These rules are complex and should you be in any doubt take regulated financial advice. For people who receive 'flexible' retirement benefits, such as a flexi-access pension (e.g. pension drawdown or taking more than 25% cash from their pension), a lower annual allowance of £4,000 also applies.

If you haven't used your full annual allowance from up to three previous years, you might be able to carry it forward and use it in the current tax year provided your earnings are high enough and you have been a member of a registered pension scheme in those preceding years. People earning more than £40,000 in the 2020/21 tax year who wish to maximise pension contributions may be able to take advantage of this.

It is also possible for non-tax payers to benefit from pension tax relief. In the 2020/21 tax year individuals under age 75 can contribute up to £2,880 to a pension and receive a further £720, resulting in an overall contribution of £3,600. In addition to upfront tax relief, money in a pension is free from capital gains tax and any income tax.

It is also important to be aware of the cap on the total value of your pensions from which you can draw benefits without triggering a tax charge (known as the "lifetime allowance"). This is £1,073,100 and is to rise with inflation. Defined benefit ('final salary') pension benefits are also tested against this limit based on the amount of income they provide when they come into payment.

Remember, should you be in any doubt about whether an investment is suitable you should seek regulated financial advice.

## Did you know?

Anyone under 75 with relevant UK earnings can receive tax relief.

# Lifetime allowance protections

If you wish to avoid the lifetime allowance charge it's important to monitor the value of your pensions, and especially the value of changes to any defined benefit pensions as these can be surprisingly large. It may also be worth applying for 'protection' if your pensions are expected to exceed the lifetime allowance threshold. This can allow you to preserve your allowance at a higher level.

If your total pension savings exceeded £1 million on 5 April 2016 there are two schemes you can apply for – Individual Protection 2016 and Fixed Protection 2016. IP2016 offers a protected lifetime allowance equal to the lower of the value of your pension savings on 5 April 2016 or £1.25 million. Meanwhile, FP2016 will fix an individual's lifetime allowance at £1.25 million instead of the standard lifetime allowance (currently £1,073,100 in the 2020-21 tax year) provided you or your employer have not added to your pension savings since 5 April 2016 and you have opted out of any work-place schemes.

The protection rules are complicated, and there are a variety of previous pension protections that have been available over the years. Having been applied for they will continue to be in place, unless they have been invalidated for some reason. Circumstances where this can happen for certain protections includes not opting out of automatic enrolment into a workplace scheme promptly, making a further pension contribution or continuing as an active member of a defined benefits scheme.

# Tax planning opportunities

Besides pensions there are other investments that attract income tax relief for individual investors, as well as capital gains tax exemption on profits. Venture Capital Trusts (VCTs) and Enterprise Investment Schemes (EIS) offer income tax relief at a rate of 30% of the amount invested provided they are held five and three years respectively. In addition, VCTs can provide a tax-free income stream from dividends, and EIS offer the ability to defer capital gains tax payable on profits from other assets. These more complex vehicles therefore offer considerable tax planning opportunities.

Where inheritance tax (IHT) is an important consideration, Business Property Relief offers an important means by which it is possible to preserve wealth for future generations. After just two years, qualifying investments, including certain unquoted investments and shares listed on the Alternative Investment Market (AIM), are exempt from IHT. We run a market leading IHT portfolio service which can reduce or potentially eliminate Inheritance Tax (IHT) as well as provide the potential for growth and income.

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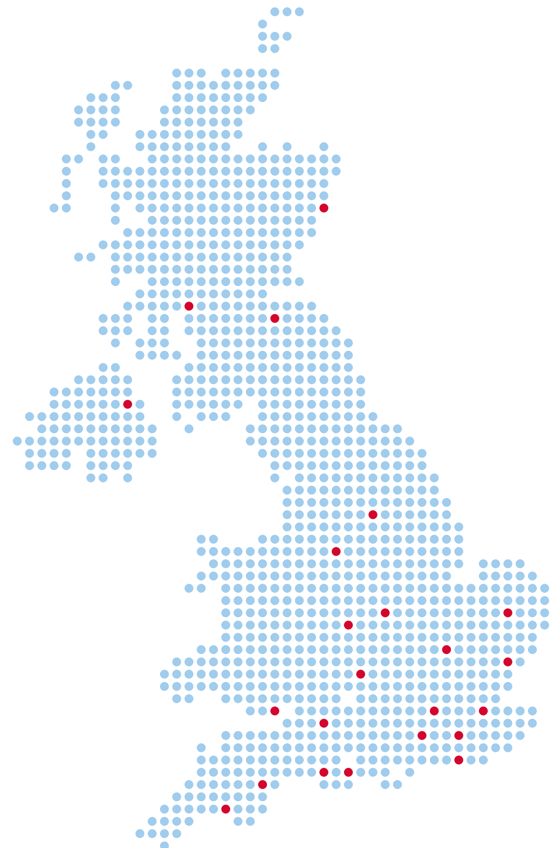

# Contact us to find out how we can help you:

At Charles Stanley our financial planners can advise you on the various ways to save tax, to help grow and preserve your wealth.

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**This guide does not constitute personal advice based on your circumstances and the contents should not be considered as a personal recommendation to deal. Investment decisions in funds and other collective investments should only be made after reading the Key Investor Information Document, Supplemental Information Document and/or Prospectus. If you are unsure of the suitability of any investment please seek professional advice.**

**The Taxation of pensions is based on individual circumstances and may be subject to change in the future. The information contained within this article is based on our understanding of current UK tax provisions, which is subject to change, and the benefits of which would depend on your personal circumstances.**

**Investors should be aware that past performance is not a reliable indicator of future results and that the price of shares and other investments, and the income derived from them, may fall as well as rise and the amount realised may be less than the original sum invested.**

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101.38B May 2020